



THE CITY OF SAN DIEGO
REPORT TO THE CITY COUNCIL

DATE ISSUED: November 29, 2006 REPORT NO. 06-187

ATTENTION: Council President and City Council
Docket of Dec. 4, 2006

SUBJECT: Agreement and Amendments to Agreements for Macias Gini & O'Connell, LLP

REFERENCE: FY 2003 – FY 2006 Financial Statement Audits

REQUESTED ACTION:

- 1) Increase in the amount of the audit of the FY 2004 basic financial statements of \$135,000 to an amount not to exceed \$850,479.
- 2) Increase in the amount of the audit of the FY 2005 basic financial statements of \$70,000 to an amount not to exceed \$914,977.
- 3) Sole source agreements with Macias in an amount not to exceed \$327,325, to reaudit the FY 2003 financial statements of the Redevelopment Agency (\$75,000); to reaudit the FY 2003 City Single Audit (\$93,600); and, to fund Macias' ongoing fraud investigation in connection with the FY 2003, FY 2004 and FY 2005 financial statement audits (\$158,725).
- 4) A sole source agreement with Macias in an amount not to exceed \$888,634 for the audit of the FY 2006 basic financial statements, which are included in the CAFR.
- 5) Authorize the Auditor and Comptroller to appropriate and to transfer up to \$1,009,229.32 from the Unallocated Reserve to the appropriate fund (see Distribution of Charges) to pay the General Fund portion (\$681,804.32) and the Public Liability portion (\$327,325) of these expenditures.

STAFF RECOMMENDATION:

Adopt the Resolution

SUMMARY:

On January 27, 2004, the City filed a voluntary financial disclosure concerning, in part, certain errors and correctible statements in the City's FY 2002 Comprehensive Annual Financial Report ("CAFR"). As a result, the FY 2003, FY 2004, and FY 2005 CAFR's have not been finalized and issued.

The City retained Macias, Gini & O'Connell, LLP (Macias) to perform the audits of the City's FY 2004 and FY 2005 basic financial statements, which are included in the CAFR's. Given the continued importance of thorough reviews, the Mayor is requesting that the City Council authorize first amendments to the contracts for the FY 2004 and FY 2005 audits and initial funding in connection with the ongoing fraud investigation. In addition initial funding for the FY2006 financial statement audit as well as initial funding for reaudits of the FY 2003 Redevelopment Agency and the City of San Diego Single Audit are being requested.

FY2004

The City retained Macias to perform the audit of the FY 2004 basic financial statements, which are included in the CAFR. The retainer was for the amount not to exceed \$715,479. The Mayor is requesting a first amendment for an additional \$135,000 to pay the services of Macias, which for the most part has already been expended. The adjustments, problems, and delays encountered in the FY2003 audit have caused Macias to perform additional work.

FY2005

The City retained Macias to perform the audit of the FY 2005 basic financial statements, which are included in the CAFR. The retainer was for the amount not to exceed \$844,977. The Mayor is requesting a first amendment for an additional \$70,000 to pay the services of Macias, which for the most part has already been expended. The adjustments, problems, and delays encountered in the FY2003 audit have caused Macias to perform additional work.

Reaudit of Redevelopment Agency

The Mayor is requesting that he be authorized and empowered to execute for and on behalf of the City, a sole source agreement with Macias in an amount not to exceed \$75,000 to reaudit the FY 2003 financial statements of the Redevelopment Agency (RDA). Caporicci & Larson, the City's former auditors, previously audited the financial statements of the RDA. Due to the significance of errors discovered by KPMG with respect to the FY2003 City audit and by Macias with respect to the FY 2004 City audit and the FY2004 RDA audit, it has been determined that the previously audited RDA financial statements are materially incorrect and must be reaudited. Macias is auditing the FY2004 financial statements and it is rational and expedient that Macias would undertake the FY2003 reaudit.

FY2003 Single Audit Reaudit

The Mayor is requesting that he be authorized and empowered to execute for and on behalf of the City, a sole source agreement with Macias in an amount not to exceed \$78,000 to reaudit the FY 2003 City

Single Audit. A Single Audit is a federally mandated audit of grantees/agencies' expenditure of Federal award monies. The Single Audit was previously audited by Caporicci & Larson, the City's former auditors. The Single Audit is inextricably tied to the CAFR audit. Because no reliance is being placed on the Caporicci & Larson audited statements, the Single Audit must be reaudited. Macias is auditing the FY2004 Single Audit and it is rational and expedient that Macias would undertake the FY2003 reaudit

Ongoing Fraud Audit

The Mayor is requesting that he be authorized and empowered to fund Macias' ongoing fraud investigation in connection with the FY 2003, FY 2004 and FY 2005 financial statement audits in an amount not to exceed \$158,725, which for the most part has already been expended. This amount represents time and materials related to the adjustments, problems, and delays encountered in the FY2003 audit and the substantial amount of time spent directly and indirectly on matters pertaining to the Audit Committee investigation and additional procedures conducted.

FY2006

The Mayor is requesting that he be authorized and empowered to execute for and on behalf of the City, a sole source agreement with Macias in an amount not to exceed \$888,634 for the audit of the FY 2006 basic financial statements, which are included in the CAFR. Macias is auditing the FY2004 and FY2005 financial statements and it is rational and expedient that Macias would undertake the FY2006 audit.

Cost Allocation

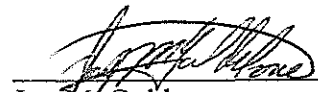
The RDA and Single Audit reaudits, as well as the ongoing fraud audit costs (a total of \$327,325) are being charged to the Public Liability Fund, Fund Number 81140. The remainder of the audit costs is being charged directly to the benefited funds under audit; the General Fund portion being \$681,804. The General Fund portion and the Public Liability portion (\$1,009,229) are both being appropriated from the Unallocated Reserve.

PREVIOUS COUNCIL and/or COMMITTEE ACTION:

The City retained Macias to perform the audit of the FY 2004 basic financial statements. Subsequently the city retained Macias to perform the audit of the FY 2005 basic financial statements.

KEY STAKEHOLDERS AND PROJECTED IMPACTS:

To return to the public finance market the City must issue its basic financial statements. In addition, to continue to be eligible for federal grants in excess of a total of \$500,000 the City must complete its federal single audits.



Jay M. Goldstone
Chief Financial Officer